

Revenue recognition, audit innovation and global airline sector update

April 2018

Presenters

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Revenue recognition



Disclosure requirements in the year of adoption

The disclosures described on the following slides are not meant to be a checklist of minimum requirements. Entities do not have to include disclosures that are not relevant or not material to them. The focus should be on meeting the objective the standard describes.

Disclosure requirements

Overview

Disclosures		
Objective	=	To enable users to understand the nature, amount, timing, and uncertainty of revenue and cash flows arising from contracts with customers
Disclosure categories	New core disclosures	Qualitative and quantitative information about: <ul style="list-style-type: none">▶ Contracts with customers▶ Significant judgments▶ Assets from capitalized costs
	Other disclosures	Other sources of new disclosures: <ul style="list-style-type: none">▶ Use of practical expedients▶ Transition disclosures (e.g., ASC 250)▶ SEC requirements (e.g., SAB Topic 11.M (SAB 74), MD&A)

Disclosure requirements

Summary

Category	Subcategory	Information type	Frequency
Contracts with customers	Disaggregation of revenue	Quantitative	Interim/annual
	Contract balances	Quantitative	Interim/annual
		Qualitative	Annual
	Performance obligations	Quantitative	Interim/annual
Qualitative		Annual	
Significant judgments	N/A	Qualitative	Annual
Contract costs	N/A	Quantitative	Annual
		Qualitative	
Other	Practical expedients	Qualitative	Annual
	Transition	Quantitative	Interim/annual
		Qualitative	
	SEC requirements	Quantitative	Interim/annual
Qualitative			

Revenue disclosures

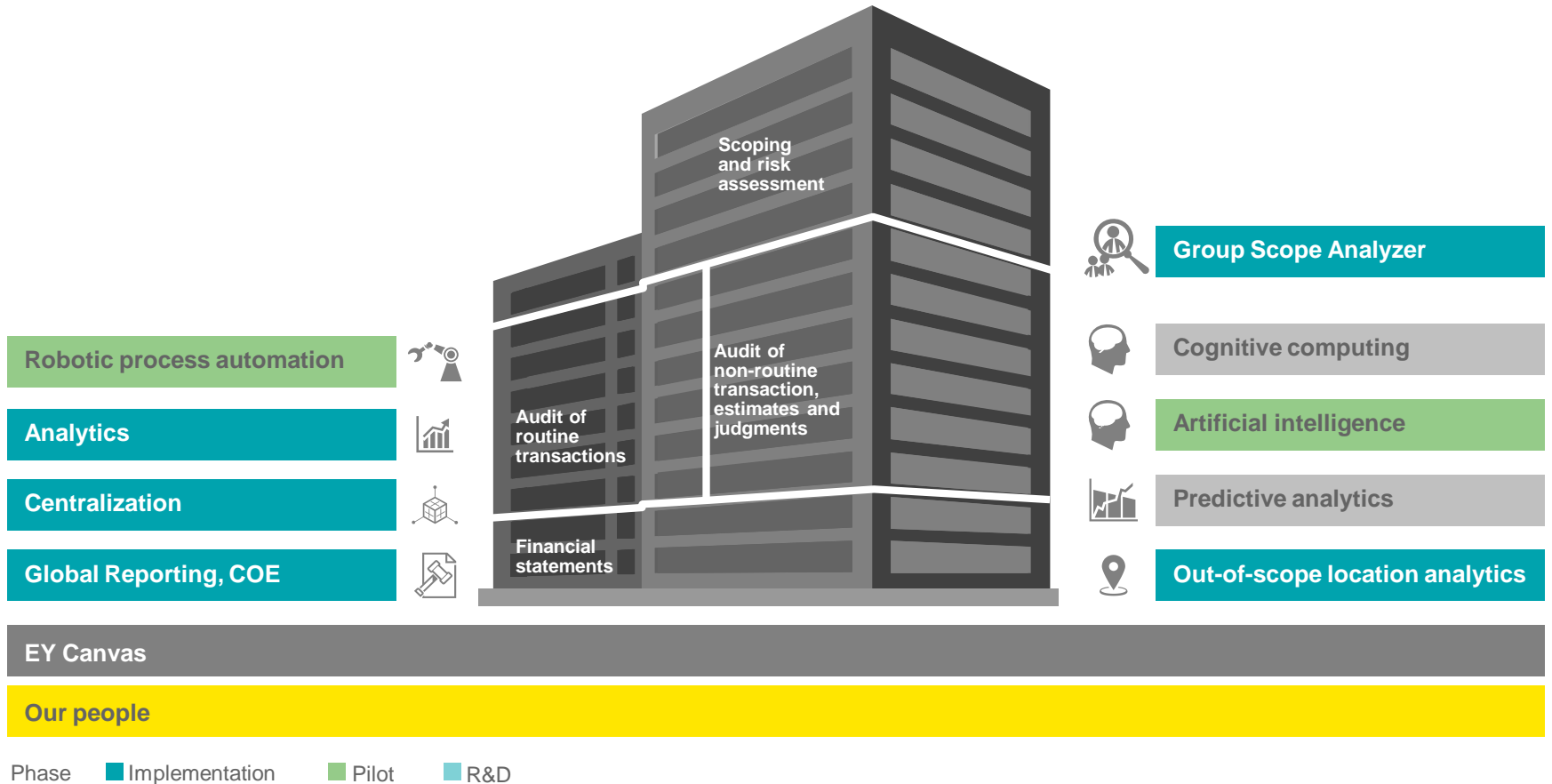
- ▶ Income statement presentation of passenger revenue
 - ▶ Most ancillary products are not separate performance obligations
 - ▶ We do not think one performance obligation should be reflected on two different lines on the income statement
 - ▶ May be willing to pre-clear with SEC
- ▶ Planned disaggregated revenue disclosures
 - ▶ Passenger, ancillary, frequent flyer redemption, frequent flyer marketing, cargo (if not already disclosed on face)
 - ▶ Ancillary may be combined with passenger in disaggregation footnote depending on facts and circumstances
- ▶ Other disclosure issues

Audit innovation – Focus on revenue



Audit innovation

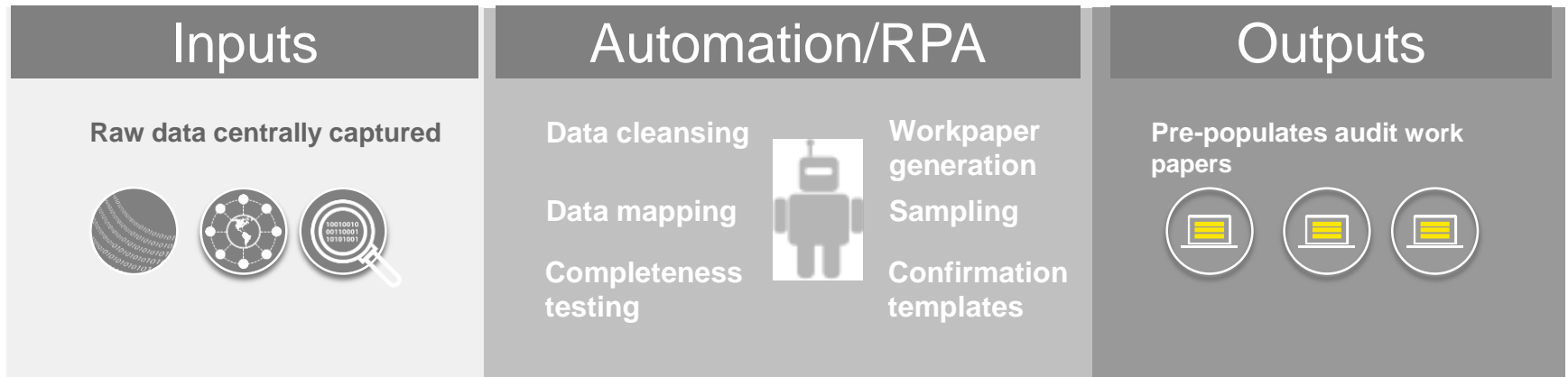
EY technology enabled audit



Audit innovation

Automation

The amplification of robotics process automation



- ✓ Allows our teams to focus on high-risk areas and value-added tasks
- ✓ Reduced burden on our teams and clients by automating data handling and processing tasks

Audit innovation

- ▶ Our global suite of data analytics is an integral element of our audits.



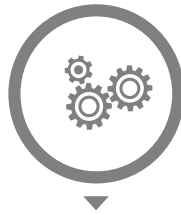
Analysis of larger populations of audit-relevant data to present **a fuller picture of the business activities** and to identify the risks that matter



Relevant feedback and insights provided during the audit to help our clients improve their business processes and controls



Clear identification of trends and anomalies in the business processes and controls to help direct our investigative effort in the right areas



Efficiencies for our clients and audit teams through insightful and targeted testing focusing on those transactions that matter most



We look for what has been cleared and what is still open.



We look at the aging of the year-end balance to understand which customers have greater risks.

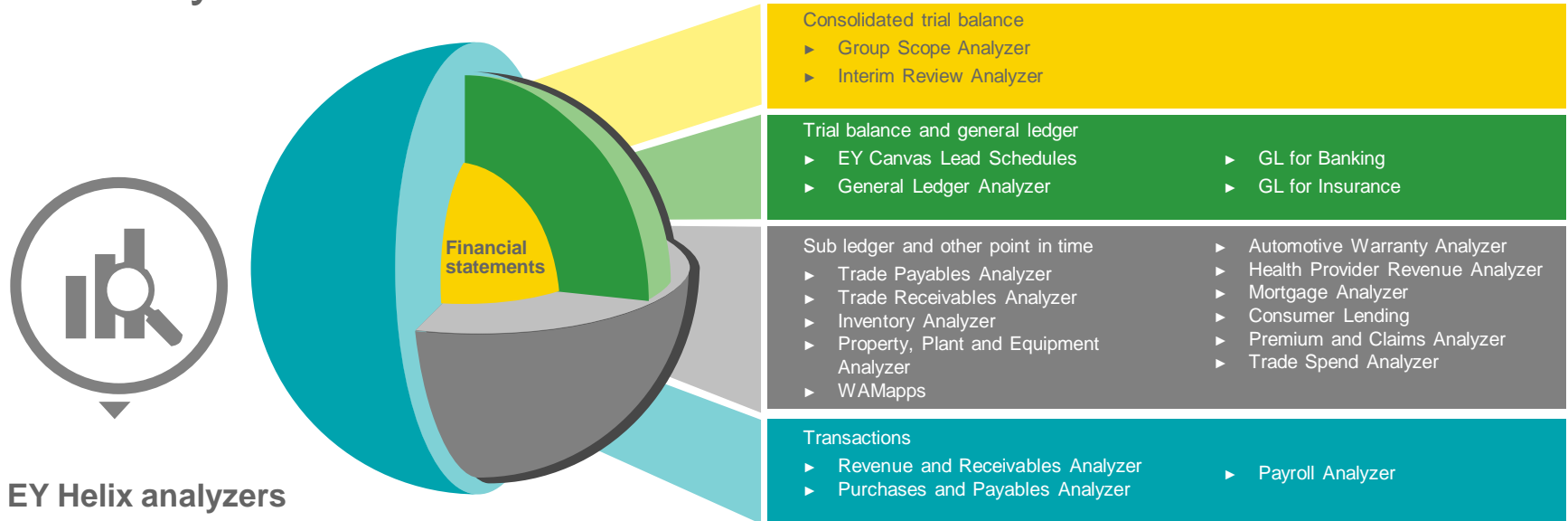
We perform additional analytics on this and on the closing balance.



Analytics at EY is not about tools looking for issues. It's about our auditors considering what the analyzed data means and assessing its implication to the audit.

Audit innovation

Data layers



EY Helix analyzers accommodate a **range of data types** so even on our biggest clients, analyzers are available for use now

Audit innovation

Global analytics platform

Data analytics across the end-to-end business operating cycle



Auditing Revenue and Receivables

General Ledger Analyzer*
Trade Receivables Analyzer
Revenue & Trade Receivables Analyzer*

Auditing Property Plant & Equipment

General Ledger Analyzer*

Auditing Payroll

General Ledger Analyzer*

Journal entry testing audit program

General Ledger Analyzer*

Auditing Trade Payables and Related Expenses

General Ledger Analyzer*
Trade Payables Analyzer
Purchases & Trade Payables Analyzer*

Auditing Inventory and Cost of goods sold

General Ledger Analyzer*
Inventory Analyzer



Revenue testing—Example

2-way correlation

Background

Industry: Retail (clothing)
Size: \$3 billion annual revenues
Inspections performed: Audit Quality Review (AQR) and Public Accounting Oversight Board (PCAOB)

Analytics performed

The team performed a test of detail using the two-way correlation analysis in EAGLe (revenue to cash) for each of its three in-scope retail locations, representing 90% of total revenue.



Results of the analysis

The correlation between revenue and cash revealed that **99.5%** of all retail revenue transactions were collected in cash. The team obtained corroborating evidence for any deviations from the expected monthly correlation (e.g., manual revenue transactions).



Effect on the audit

- ▶ The team concluded that it had obtained persuasive audit evidence over the occurrence of revenue.
- ▶ No additional tests of transactions were performed.
- ▶ Eliminated the testing of 120 transactions across the three components.
- ▶ Approach saved the client 60 hours of pulling supporting documentation.

Inspection results

The team walked the inspectors through the testing approach ahead of the review and answered questions about the completeness and accuracy of the data (i.e., Information provided by the entity (IPE)).

AQR and PCAOB inspectors took no exception to the team's approach or level of evidence obtained from the analytic procedures.



Airline example

Traditional ticket testing

- ▶ Sample based approach vs. holistic

Standard passenger revenue-related entries:

- ▶ Sale
 - ▶ Debit AR
 - ▶ Credit deferred revenue
- ▶ Cash collection
 - ▶ Debit cash
 - ▶ Credit AR
- ▶ Revenue recognition on lift
 - ▶ Debit deferred revenue
 - ▶ Credit revenue

Airline example, continued

- ▶ High correlation among AR → Deferred Revenue → Revenue
 - ▶ Can explain most variations like interline activity, cash sales, etc.
 - ▶ Still material items to investigate, but focus is on the risk
- ▶ Controls reliance
 - ▶ Control reliance and test of details to test AR and cash balances

Global airline sector update



Global airline sector update

Operating margins are still high for the industry but stabilizing even though rising jet fuel prices and unit costs pose the biggest challenge.



Global airline sector update

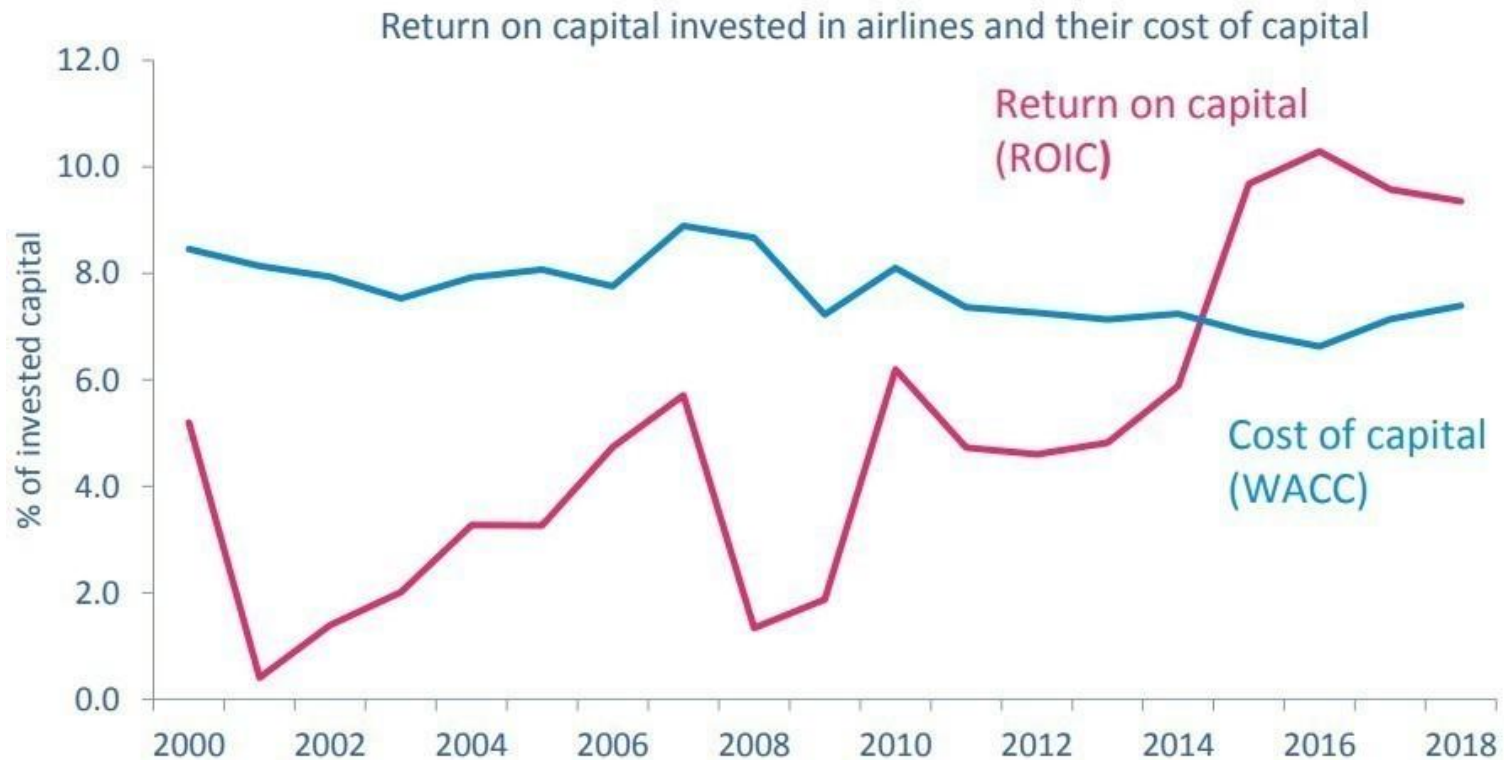
The 2017 results are slightly down from 2016, with softening in the US and Asia-Pacific largely offset by improvements in Europe. Forecasts for 2018 include a growth in profits across most regions.

Composition by region of net profit							
(In US\$ billions)	2018F	2017	2016	2015	2014	2013	2012
North America	16.4	15.6	16.5	21.7	11.1	7.4	2.3
Europe	11.5	9.8	8.8	7.5	1.9	1.0	0.4
Asia-Pacific	9.0	8.3	8.1	7.3	0.3	2.3	5.8
Latin American	0.9	0.7	0.7	(1.6)	0.0	0.2	(0.2)
Middle East	0.6	0.3	1.3	2.1	1.1	0.3	1.0
Others	(0.1)	(0.1)	(0.1)	(1.0)	(0.8)	(0.5)	(0.1)
Total	38.4	34.5	35.3	35.9	13.7	10.7	9.2

Source: IATA

Global airline sector update

Overall return on capital lower in 2017 and seems to be declining as the cost of capital is rising from 2016 onward.



Source: IATA

Global airline sector update

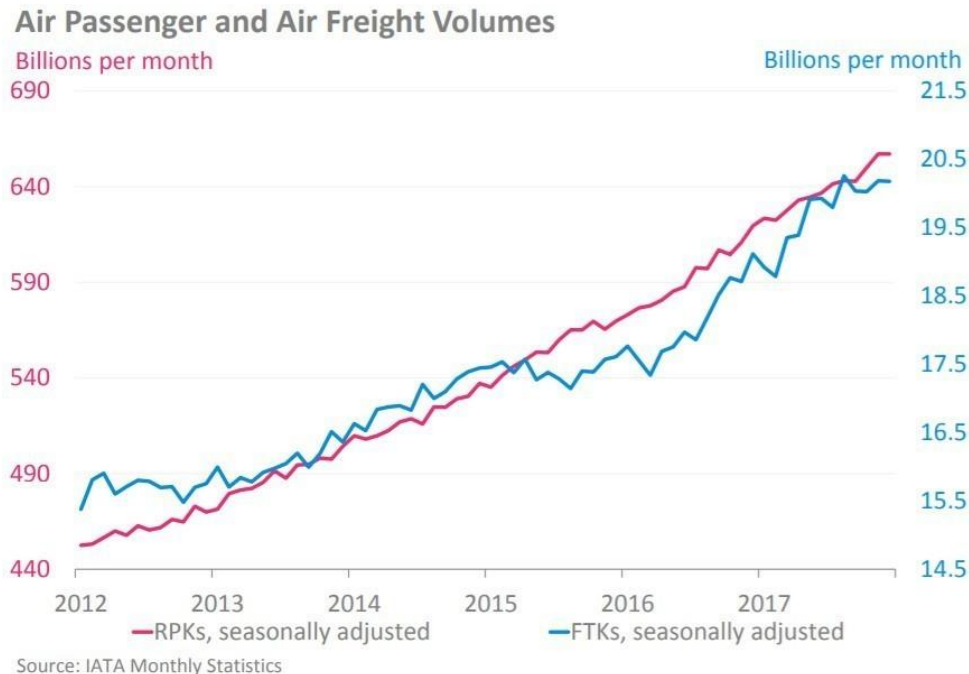
Capacity has grown across all regions with an equivalent increase in demand, except North America or the Middle East where capacity is outpacing demand.

	Dec. 2017 vs. Dec. 2016		2017 vs. 2016	
	Demand (RPK)	Capacity (ASK)	Demand (RPK)	Capacity (ASK)
North America	4.0%	4.2%	4.2%	4.1%
Europe	6.1%	4.4%	8.2%	6.2%
Asia-Pacific	9.1%	8.3%	10.1%	8.4%
Latin America	5.4%	5.0%	7.0%	5.5%
Middle East	3.4%	5.7%	6.4%	6.5%
Others	3.4%	2.6%	6.3%	2.9%

Source: IATA

Global airline sector update

Growth in industry-wide passenger volume increased by 7.6% YoY whereas global freight volumes grew by 9.0% in 2017; however, there was a moderate slowdown in passenger growth in 2018 as stimulus to demand from lower airfares declines.



Source: IATA

Global airline sector update

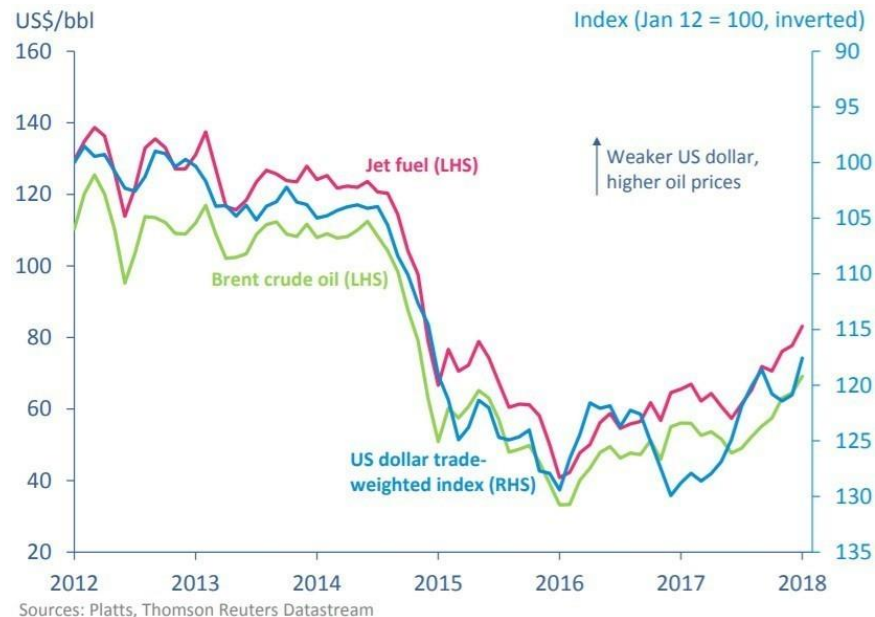
Passenger yields are expected to rise modestly during 2018 with expected robust economic growth, even though financial markets have been volatile recently and input costs have increased.



Source: IATA

Global airline sector update

Brent crude oil price rose to a three-year high during January, continuing the upward trend that started in mid-2017, supported by OPEC-led production cuts and a weaker US dollar; net impact of reduced supply from OPEC and increasing supply from US.



Source: IATA

Global airline sector update

Fuel prices globally have increased in 2017

2 March 2018	Share in World Index	cts/gal	\$/bbl	\$/mt	Index Value 2000 =100	vs. 1 week ago	vs. 1 month ago	vs. 1 yr ago
Jet Fuel Price	100%	188.3	79.1	623.6	216.2	-4.2%	-6.0%	21.9%
Asia & Oceania	22%	188.9	79.3	626.7	226.7	-2.5%	-6.4%	20.5%
Europe & CIS	28%	193.0	81.0	638.6	218.4	-4.7%	-3.5%	24.5%
Middle East & Africa	7%	186.2	78.2	617.0	233.5	-3.9%	-5.3%	22.6%
North America	39%	184.7	77.6	612.9	206.3	-4.9%	-7.6%	21.1%
Latin & Central America	4%	190.3	79.9	615.4	221.4	-5.3%	-7.5%	18.9%

Jet fuel price average for 2018

\$81.6/bbl

Impact on 2017 fuel bill

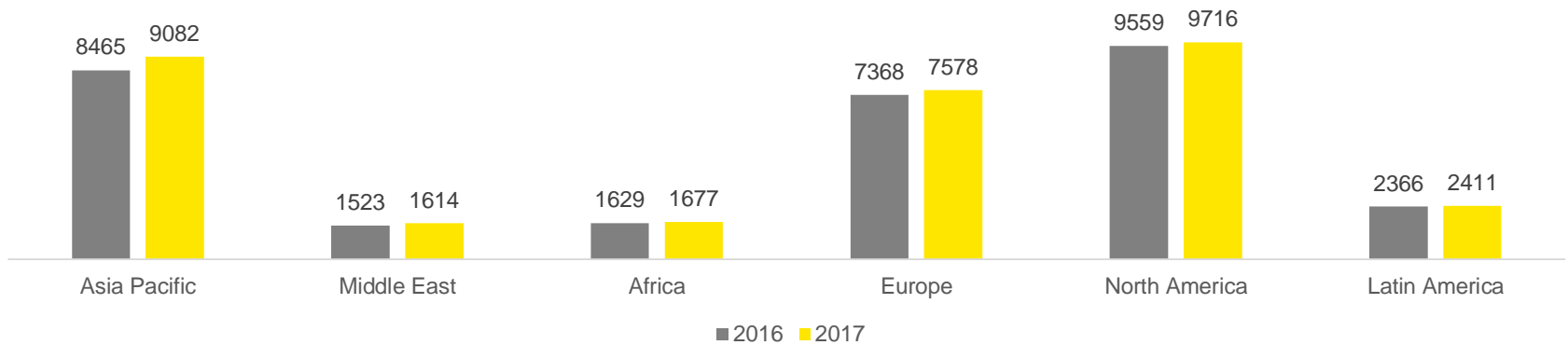
\$34.8b

Source: IATA, Platts

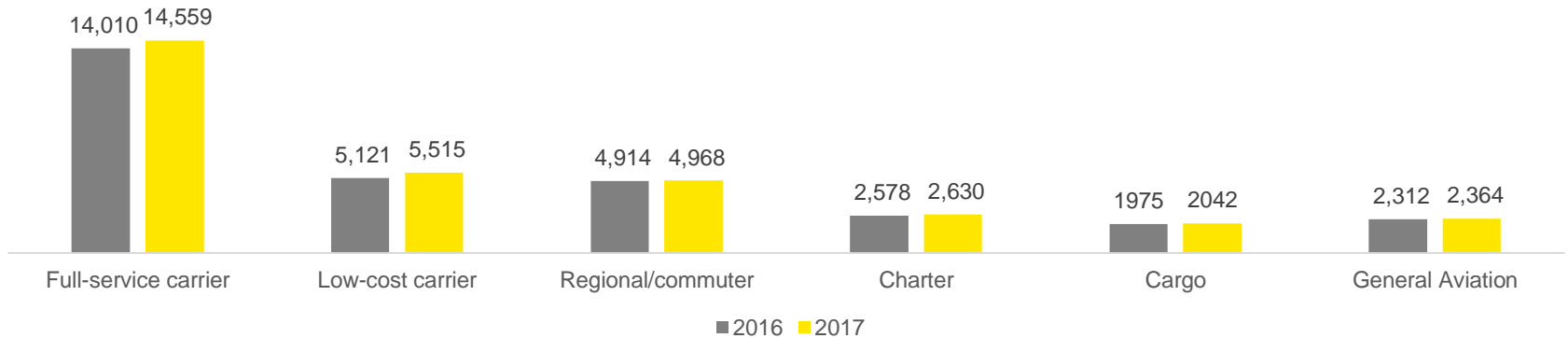
Global airline sector update

Global fleet size by region and business model

Global fleet by region



Global fleet by business model

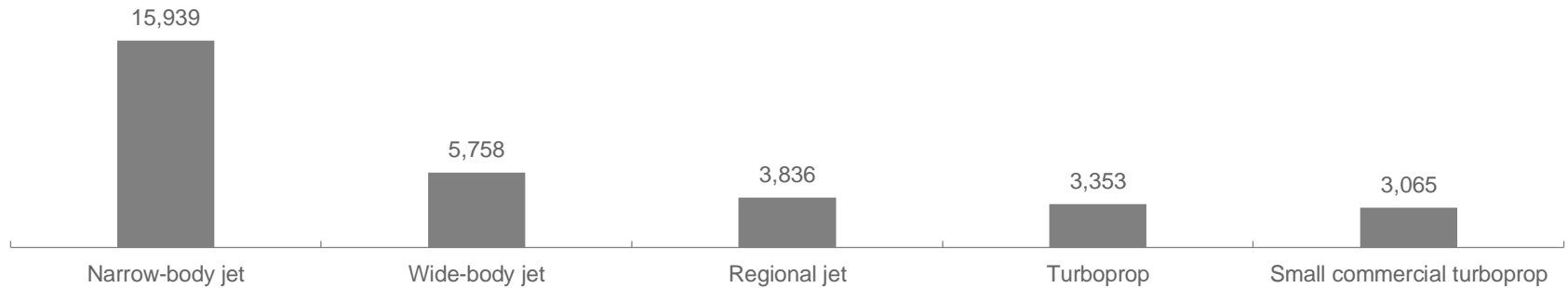


Source: CAPA

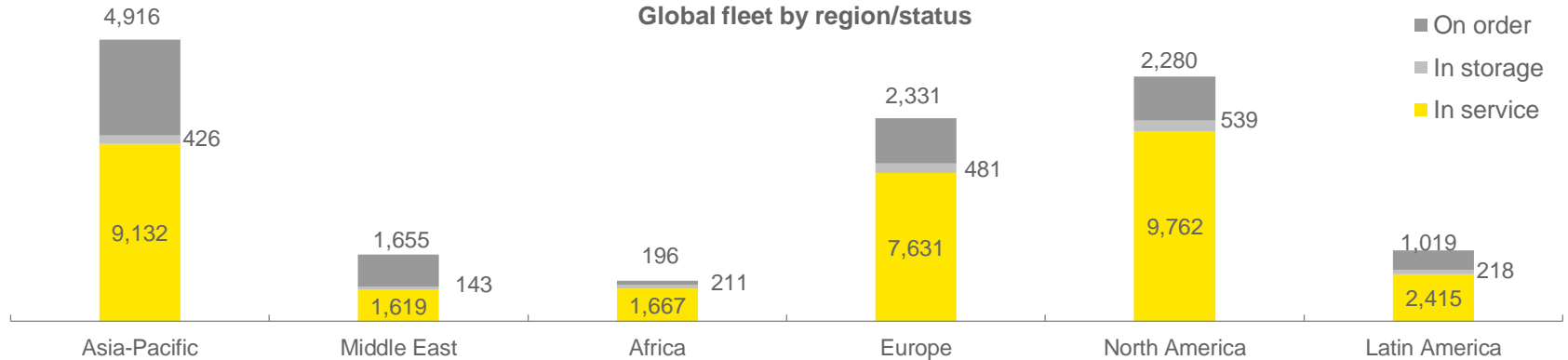
Global airline sector update

Global fleet size by aircraft type and region/status

Global fleet by aircraft type



Global fleet by region/status



Source: CAPA, as of March 10, 2018

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